



4th quarter 2009

Tennessee Housing Market

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Economic Overview

The growing national economy has not yet produced visible relief for Tennessee. Although the recession has likely ended from an economist's perspective, improving conditions have not yet resulted in job growth. Employment continued to decline during the fourth quarter, posting losses in every industry except health care and social services.

Initial claims for unemployment insurance declined (Fig. 1), signaling that employers are laying off far fewer workers than earlier in 2009. However, fewer layoffs have not led to additional hiring. The Tennessee unemployment rate dropped (Table 1), but this was caused by a decline in the labor force: fewer people are looking for work. Employers are very cautious about hiring given the level of uncertainty regarding demand for goods and services.

Some positive signs can be found in the manufacturing sector nationally. The Purchasing Managers Index (PMI), an indicator of manufacturing strength, rose for the sixth straight month, signaling an expanding manufacturing sector.

Average weekly hours worked in manufacturing are up for the U.S. and Tennessee, as is hiring in the temporary help sector. Both can be considered leading indicators of manufacturing employment growth.

Housing Construction

Single-family home construction permits rose again in the fourth quarter, climbing to 13,500 from 12,700 in the third quarter. Although single-family construction has improved for four consecutive quarters, the level of activity remains substantially lower than most of 2008 (Table 2 and Fig. 2).

Compared with the Southern states and the U.S., however, Tennessee's single-family construction is progressing more rapidly. Single-family permits increased 6.6% in the fourth quarter for Tennessee, compared with just 2.5% for the South and 3.2% for the U.S.

In contrast with the single-family market, multi-family construction remains in the doldrums. Although multi-family permits rose in the fourth quarter, they remain at an extremely low level. Tightened credit markets have all but dried up lending for these units.

Table 1. Selected Tennessee employment indicators (in thousands, seasonally adjusted)

	2008.4	2009.1	2009.2	2009.3	2009.4
Employment by industry (nonfarm)					
Total nonfarm	2,743.0	2,696.4	2,659.2	2,653.4	2,643.2
Goods-producing sectors	478.8	448.5	428.9	424.2	420.1
Manufacturing	350.0	332.1	320.0	320.0	318.6
Services-providing sectors	2,264.2	2,248.0	2,230.3	2,229.3	2,223.1
Unemployed	220.6	275.6	317.7	320.9	309.0
Total employment	2,826.9	2,765.9	2,721.9	2,692.0	2,675.8
Labor force	3,047.4	3,041.5	3,039.6	3,012.9	2,984.8
Unemployment rate	7.2%	9.1%	10.5%	10.7%	10.4%

Source: Bureau of Labor Statistics

Figure 1. Tennessee initial claims for unemployment insurance (quarterly averages of weekly data, seasonally adjusted)

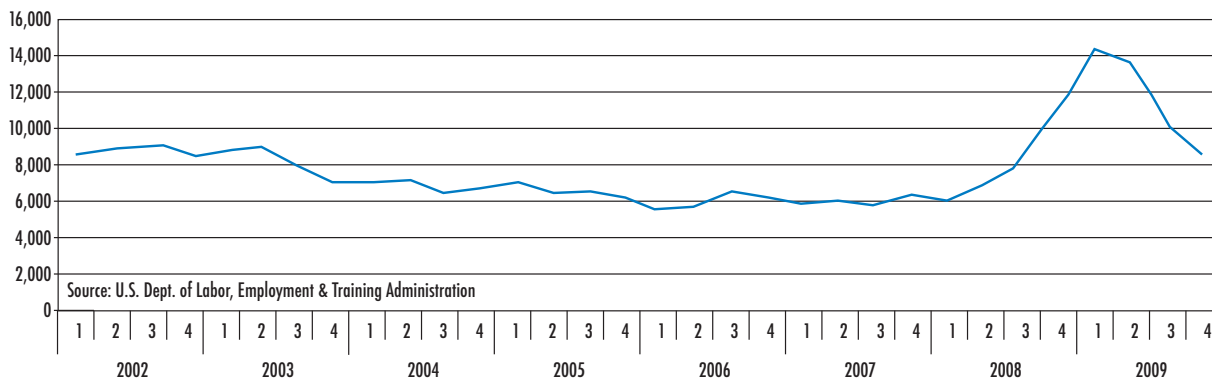


Table 2. Permits issued for privately owned new housing (seasonally adjusted annual rate, in thousands)

Source: Census Bureau

Quarter	Single-Family Permits			Multi-Family Permits			Total Permits		
	Tennessee	South	U.S.	Tennessee	South	U.S.	Tennessee	South	U.S.
2007.2	29.4	528.3	1,031.7	7.4	204.3	425.0	36.7	732.7	1,456.7
2007.3	27.1	474.7	916.3	6.6	163.3	398.0	33.7	638.0	1,314.3
2007.4	22.5	414.0	786.0	8.4	175.3	402.3	30.9	589.3	1,188.3
2008.1	18.4	364.0	670.0	5.5	174.0	358.3	23.9	538.0	1,028.3
2008.2	17.4	327.7	627.0	3.6	154.3	420.7	21.0	482.0	1,047.7
2008.3	15.4	286.3	550.7	5.8	159.3	311.7	21.3	445.7	862.3
2008.4	9.9	219.7	420.7	4.7	104.3	220.3	14.7	324.0	641.0
2009.1	10.5	198.7	361.0	2.7	79.0	169.7	13.2	277.7	530.7
2009.2	11.1	213.0	405.7	3.9	64.0	123.0	15.1	277.0	528.7
2009.3	12.7	242.3	459.7	1.2	46.3	113.3	13.9	288.7	573.0
2009.4	13.5	248.3	474.3	1.4	50.7	123.3	14.9	299.0	597.7
Change from previous quarter	6.6%	2.5%	3.2%	14.1%	9.4%	8.8%	7.2%	3.6%	4.3%
Change from previous year	35.9%	13.1%	12.8%	-70.0%	-51.4%	-44.0%	1.7%	-7.7%	-6.8%

The moderate but steady rise in single-family construction activity has been aided by extremely low mortgage rates, the first-time buyer's tax credit, and Federal Reserve purchases of mortgage securities from Fannie Mae and Freddie Mac. Policy support of the mortgage market is changing, however. The tax credit is set to expire at the end of April, and the Fed has announced plans to begin reducing its mortgage holdings, which will put upward pressure on mortgage rates. Further, the FHA has announced plans to tighten lending requirements in order to reduce unexpectedly high future loan losses. The combined effect of these policy changes will be to reduce demand for housing to a lower level than otherwise would have occurred.

Real Estate Transactions and Mortgages

Taxes collected on real estate transfers rose for the second consecutive quarter, albeit modestly, gaining 2.2% from the third quarter (Fig. 3). The transfer tax is based on the value of a property transaction; the small fourth-quarter gain likely means that although more property is changing hands, the property value is lower than just a few months ago. That being said, Tennessee has not experienced two consecutive quarterly gains since 2006. The second housing-related tax, the mortgage tax, gained 7.5% in the fourth quarter following two months of decline (Fig. 4). The higher mortgage tax collections signal increased borrowing activity for both new and pre-existing home purchases.

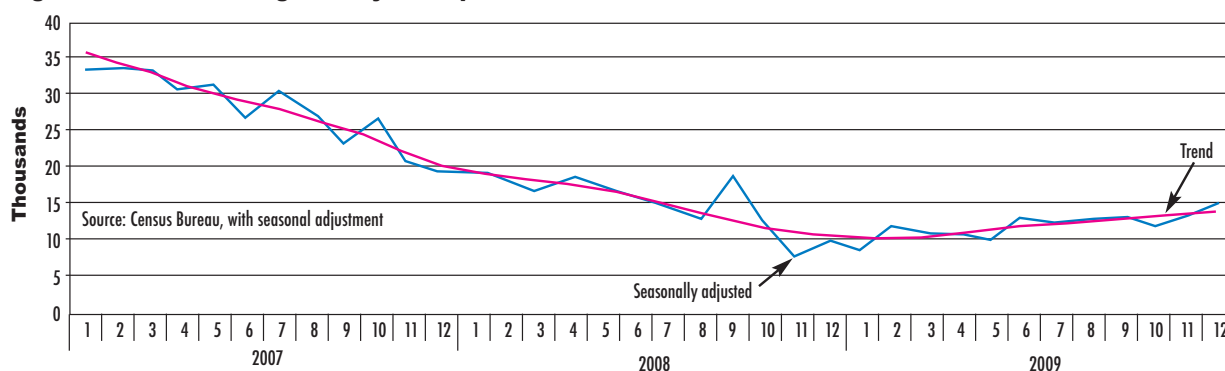
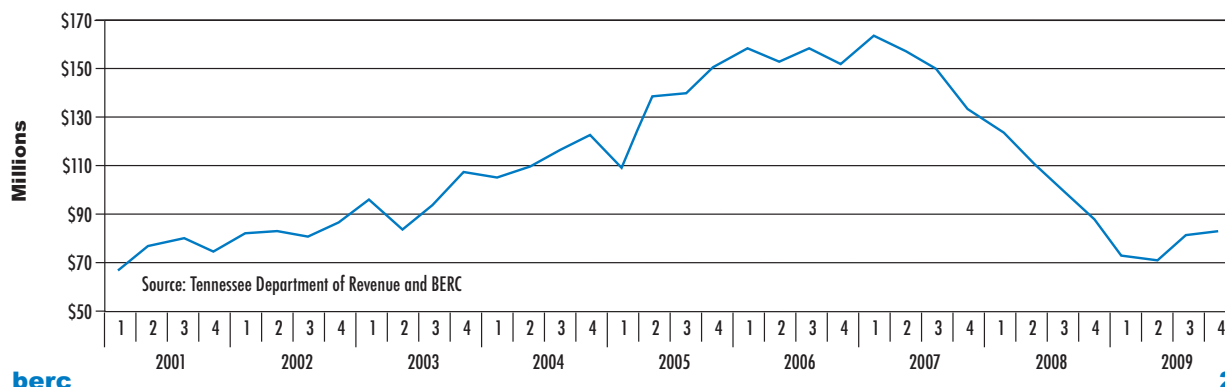
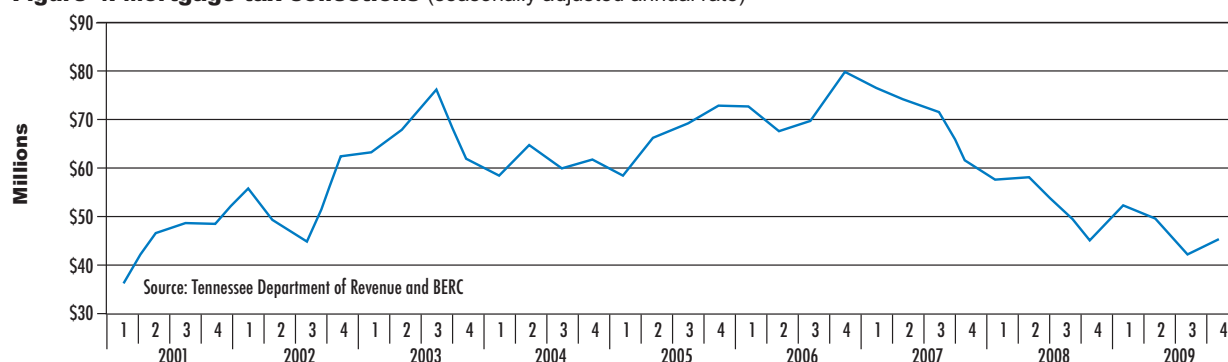
Figure 2. Tennessee single-family home permits**Figure 3. Real estate transfer tax collections** (seasonally adjusted annual rate)

Figure 4. Mortgage tax collections (seasonally adjusted annual rate)

Home Sales

Sales of single-family homes rose sharply in the Nashville, Memphis, and Knoxville areas (Fig. 5-7) for the third consecutive quarter. Sales are 20% higher for Nashville, 9.8% for Memphis, and 16.9% for Knoxville. Inventories of homes on the market dropped modestly in Nashville and Memphis but are level in Knoxville. Sales for Nashville and Knoxville are the highest since the first quarter of 2008, while Memphis sales are the highest since the third quarter of 2008.

Maintaining improvement in the housing market will require housing price stability and employment growth. Housing prices are experiencing considerable downward pressure in Tennessee; according to Federal Housing Finance Agency data, housing prices are 2.2% lower over the year for Tennessee, 2.1% lower for Nashville, down 2.2% for Memphis, and 0.9% lower for Knoxville. To be sure, other areas of the nation such as Florida, Nevada, Arizona, and California are experiencing much more housing price deflation. U.S. average housing prices in the third quarter 2009 declined 3.8% over the year. Given the continuing rise in foreclosures (below), price stability is not yet in sight.

We continue to search for employment growth in Tennessee. While the number of layoffs has trended lower over the past 12 months, net job creation has not followed. Job growth is needed to boost confidence and spur in-migration from other counties and states, one of the driving forces in Tennessee's housing growth.

Mortgage Delinquencies and Foreclosures

Mortgages past due and new foreclosures show no sign of abating, according to the latest Mortgage Bankers Association fig-

ures (Table 3). The number of foreclosures initiated during the third quarter of 2009 exceeded 1% in Tennessee for the first time during this downturn. Rising foreclosures are a symptom of the continuing severe financial stress felt by many Tennessee households in the face of higher unemployment and income losses. The fact that conditions are worse and unraveling faster for the U.S. provides a little comfort for Tennessee.

As has been the case during this recession, Tennessee ranks very high in the percent of mortgages past due (8th highest) but about average for the percent of new foreclosures (24th highest). As for seriously delinquent mortgages,¹ Tennessee's third quarter 2009 figure is 6.53%, ranking near the middle (23rd highest) among the 50 states. By comparison, states with the most severe housing problems (Michigan, Arizona, Florida, California, Nevada) are experiencing seriously delinquent rates from 10% to 18%. The lowest seriously delinquent mortgage rates are found in the west central states stretching from Texas to the Canadian border, which average about 5.5%.

Conclusion

Some signs of improvement continue for Tennessee's housing market: residential sales, single-family construction permits, and real estate transactions are up. However, rapidly increasing numbers of foreclosures and distressed mortgages will put additional downward pressure on housing prices. Job creation is needed to solidify recent housing market gains. Job growth remains elusive, but we see signs of improvement, particularly in manufacturing.

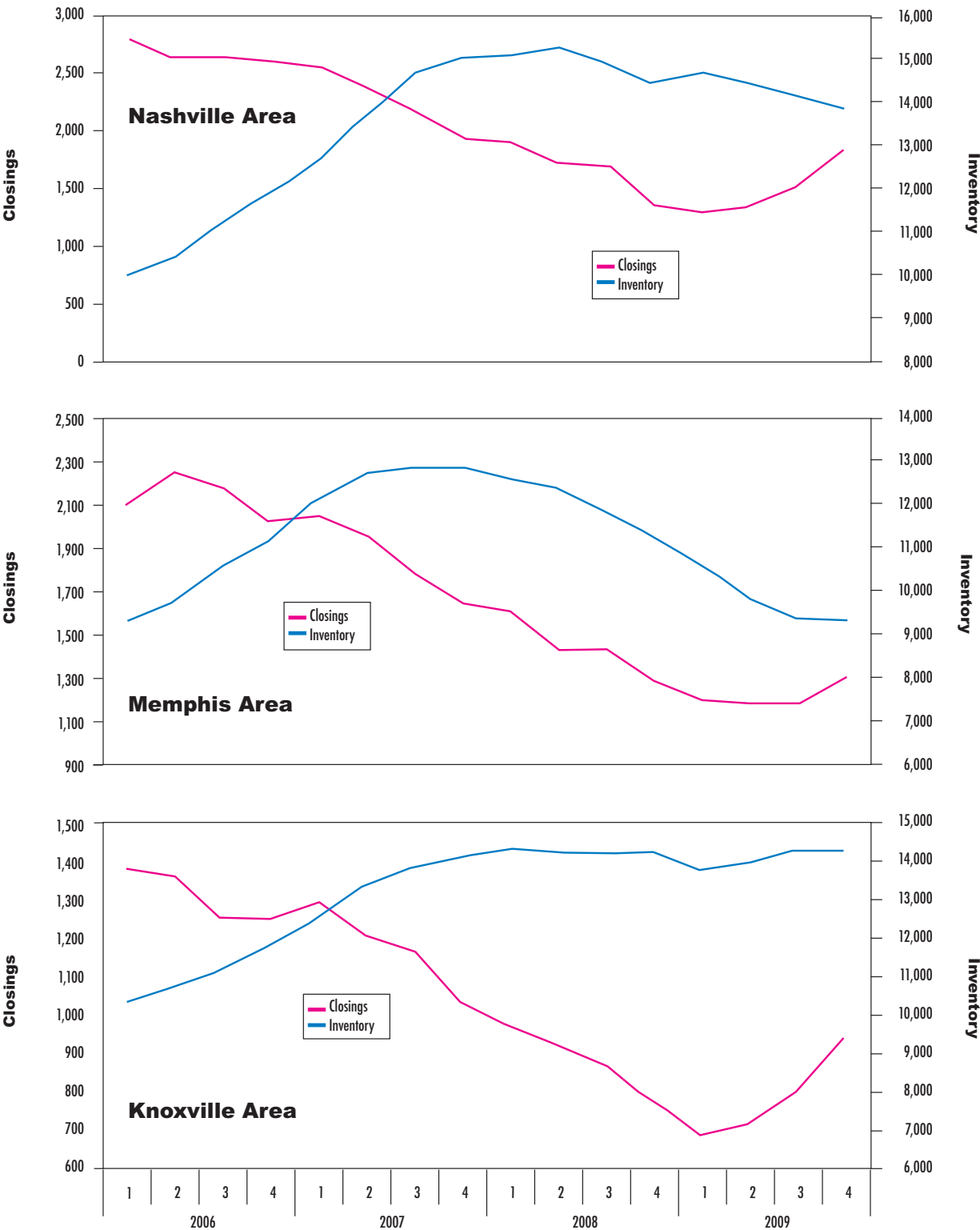
¹ According to the Mortgage Bankers Association, seriously delinquent mortgages are the sum of mortgages at least 90 days past due plus the current inventory of foreclosures, as a percent of all mortgages in service.

Table 3. Mortgages past due, new foreclosures started, foreclosure inventory (% of mortgages serviced, seasonally adjusted)

Quarter	Tennessee			U.S.		
	Mortgages past due	Foreclosures started during quarter	Foreclosure inventory at end of quarter	Mortgages past due	Foreclosures started during quarter	Foreclosure inventory at end of quarter
2007.3	7.41	0.69	1.30	5.60	0.78	1.72
2007.4	7.34	0.72	1.38	5.79	0.85	2.01
2008.1	7.74	0.71	1.48	6.21	0.99	2.42
2008.2	7.95	0.77	1.55	6.45	1.14	2.79
2008.3	8.41	0.78	1.61	7.03	1.08	3.02
2008.4	9.08	0.81	1.73	7.91	1.04	3.26
2009.1	10.08	0.93	1.95	9.04	1.33	3.77
2009.2	10.31	0.99	2.21	9.21	1.43	4.36
2009.3	10.71	1.03	2.30	9.59	1.44	4.55

Source: Mortgage Bankers Association of America, BERC

Figure 5. Single-family sales and inventory (seasonally adjusted quarterly average of monthly figures)



Source: Greater Nashville Association of Realtors, Memphis Area Association of Realtors, Knoxville Area Association of Realtors, and BEREC